

South Dakota

State Brand Board

Feasibility Study

Final Report
Prepared by

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Background of Study

The South Dakota State Brand Board (SDSBB) sent a Request for Proposals out on October 3, 2007. John Meetz a Consultant from Wichita, Kansas, submitted a proposal on November 5, 2007. The proposal was approved by the SDSBB and a contract was executed on November 28, 2007, and signed by John Meetz.

The study was initiated due to contract negotiations that occurred in early 2007 between the SDSBB and the South Dakota Stockgrowers' Association (SDSGA) who contracts with the SDSBB to provide brand inspection services in the western part of South Dakota. At times during those negotiations it appeared that an agreement on contract terms may not be reached. The SDSBB according to State Law is required to provide brand inspection service to the industry in the "West River Brand Inspection Area" of the State. If contract negotiations had failed, the SDSBB did not have a back up plan or "Plan B". Therefore this feasibility study was initiated to better understand the options for the SDSBB to meet the requirements for brand inspection under State Law.

The expectations and scope of services of the feasibility study are outlined in the Request for Proposal and in Exhibit A of the contract with the Consultant and are as follows.

Scope of Services

The scope of services to be rendered to the Board by the Consultant will include, but not limited to, developing a complete plan for funding, staffing and operating the livestock ownership inspection program as a function of the Board. Factors to be considered in the development of the plan include the following:

1. Obtain input from the various interested parties in the livestock industry on the brand inspection program to insure their needs are addressed in the development of the program and to assess where improvements in service quality may be possible;
2. Recommend the number and type of management and staff necessary to perform livestock ownership inspections, the appropriate locations to place staff to perform those services, and the appropriate supervisory structure between the current Brand Board personnel and the additional staff necessary to perform those services;
3. Develop recommendations acquiring the necessary office space, vehicles, equipment, supplies and other items needed for conducting the inspection program;
4. Work with the SD Bureau of Personnel to establish appropriate job classifications and compensation and benefits packages for the necessary staff;

5. Assess feasibility of retaining current inspection personnel to fill the staff positions;
6. Develop standard operating policies and procedures for the management and operation of the livestock ownership inspection program by the Board;
7. Prepare financial projections of the anticipated initial and ongoing costs of operating the livestock ownership inspection program;
8. Develop the fee structure necessary to fund the ongoing costs of operating the livestock ownership inspection program, including establishment of cash flow reserves;
9. Identify a source of funding for the initial startup costs of the program;
10. Develop a plan for the changeover of the program from the private contractor to the Board, and make recommendations on the timing of the changeover;
11. Make recommendations for notifying the interested parties in the livestock industry of the method and timing of the changes in the livestock ownership inspection program, and of the potential impact of the changeover to those interested parties; and
12. Examine whether the services being provided in connection with the livestock ownership inspection program, either as presently conducted or as conducted after a changeover, still provide value to the livestock industry and are conducted with proper timing and in the most efficient manner.

History and Brand Laws

In 1880 the first brands were published in the Black Hills Weekly Journal. The first state brand law was passed by the Legislature and signed by the Governor in 1897.

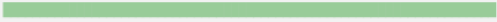
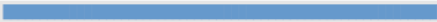




The State has never required producers to brand their livestock in the West River Brand Inspection Area or any other part of the State. However if a hot iron brand is used by a producer it must be registered with the SDSBB. Registered brands must be renewed every five years in years ending with a 5 or 0.

A survey was conducted of South Dakota producers and feeders in the Fall of 2006 as a part of the South Dakota State Beef Study. One of the questions in the survey asked what form of identification producers used in their operations. The answer shows the use of branding by region in the State. As expected, the Western Region (West River) uses brands more than any other region of the state with 83.3% of producers using brands as a means of identifying their cattle. The other areas of the State east of the river varied between 27.3% in the East Central Region and 11.1% in the Southeast Region.

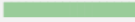
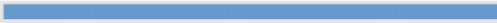




The following question was asked of producers and the graphs show the results by region of the State. Respondents could check all that applied to their operation.

What form of animal identification do you utilize on your market steers/heifers?

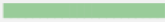
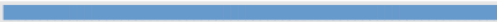





Western (West River) Region

Brand		83.3%	345
Ear tag		72.9%	302
Metal clip		5.1%	21
RFID tags		5.8%	24
Tattoo		8.5%	35
Retinal scan		0%	0
None		3.9%	16
Total # of respondents 1184. Statistics based on 414 respondents; 752 filtered; 18 skipped.			


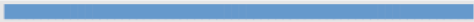




Northeast Region

Brand		23.2%	51
Ear tag		87.3%	192
Metal clip		6.4%	14
RFID tags		7.7%	17
Tattoo		9.1%	20
Retinal scan		0%	0
None		10%	22
Total # of respondents 1184. Statistics based on 220 respondents; 946 filtered; 18 skipped.			

East Central Region

Brand		27.3%	80
Ear tag		86.7%	254
Metal clip		6.8%	20
RFID tags		7.8%	23
Tattoo		10.6%	31
Retinal scan		0.3%	1
None		6.8%	20
Total # of respondents 1184. Statistics based on 293 respondents; 873 filtered; 18 skipped.			

Southeast Region

Brand		11.1%	25
Ear tag		79.2%	179
Metal clip		3.5%	8
RFID tags		8.4%	19
Tattoo		7.5%	17
Retinal scan		0%	0
None		17.3%	39
Total # of respondents 1184. Statistics based on 226 respondents; 940 filtered; 18 skipped.			

State law requires all cattle and horses to be inspected if they leave the Brand Inspection Area which is defined in State Law to include the following counties or all of the State located west of the Missouri River.

§ 40-20-1. Counties included in inspection area.

The South Dakota livestock ownership inspection area consists of all of that part of the State of South Dakota lying within the following counties: Harding, Butte, Lawrence, Pennington, Custer, Fall River, Perkins, Meade, Shannon, Corson, Dewey, Ziebach, Haakon, Stanley, Jackson, Jones, Mellette, Bennett, Todd, Lyman, Tripp, and Gregory.

The basic authority granted to the SDSBB is stated in the following statutes:

§ 40-18-10. Designation of private or nonprofit corporation for provision of ownership inspection -- Terms of contract.

The board may designate as an agency for the carrying on of livestock ownership inspection work a private or nonprofit corporation, and fix the compensation. Any contract entered into for the provision of livestock ownership inspection work shall contain provisions requiring a separate accounting of all income received and expenses paid by the agency based on such contract. Such accounting information shall be available to the public upon request to the board.

§ 40-18-15. Ownership inspection on transportation of livestock.

The board may inspect all livestock moved within the South Dakota livestock ownership inspection area and all livestock leaving the South Dakota livestock ownership inspection area for the purpose of determining the proper ownership and brands, if any, of such livestock and shall have general charge, supervision, and custody of all instruments, records, and files in connection with such ownership inspection activities.

§ 40-18-16. Rules promulgated by board.

The board may promulgate rules pursuant to chapter 1-26 to:

- (1) Describe prohibited brand symbols for various types of livestock and identify locations on animals where a brand is permitted;
- (2) Provide for the registration, transfer, and renewal of livestock brands;
- (3) Establish a brand registration fee not to exceed twenty-five dollars;
- (4) Establish a brand renewal fee not to exceed ten dollars per year or a brand renewal fee not to exceed fifty dollars for each five-year ownership period and a brand transfer fee not to exceed twenty-five dollars;
- (5) Establish an ownership inspection fee not to exceed eighty cents for each head of livestock;

- (6) Establish recordable livestock brands;
- (7) Establish law enforcement, ownership inspection, and transportation requirements within or without the ownership inspection area;
- (8) Establish a duplicate certificate fee not to exceed five dollars;
- (9) Establish a mileage fee for inspectors not to exceed the rate set by the State Board of Finance.

§ 40-18-17. Board to provide for brand registration, livestock inspection, and enforcement of laws.

The Brand Board shall provide for the registration of livestock brands, for the inspection of livestock for ownership identification purposes, and for the enforcement of laws pertaining to the inspection, sale, branding, ownership, transportation, and theft of livestock within the ownership inspection area and the state.

(Note – The law was recently amended in point (5) above to say the ownership inspection fee may not exceed \$1.00 for each head of livestock)

The SDSBB has contracted with the South Dakota Stock Growers Association basically since the beginning of Brand Inspection in the State. A number of times in the past there have been serious deliberations regarding moving the brand inspection program to the SDSBB. Recently various political circumstances (to be discussed later in this report) and questions regarding the integrity of the program have strained the relationship between the SDSBB and the SDSGA which were all part of the rationale for this feasibility study.

Analysis of Information

The Consultant for this project was provided financial and other information from the SDSBB and the SDSGA as background information and to help prepare this report. The contract between the two organizations runs from July 1 to June 30. In the past, the basic contract provided for the SDSGA to provide the brand inspection service at markets and locals (on the ranch for animals that are going to leave the brand inspection area but are not going through a market in the brand inspection area). The Association collected the brand inspection fees and paid all expenses. If the service made money the SDSGA kept the profits and if it lost money the Association stood the loss.

In contract negotiations in the Spring of 2007 the SDSBB wanted more transparency of the fees being collected and the expenses being paid. Thus under the new contract all fees go into a separate bank account of the SDSBB and checks for expenses are written on that account by the SDSGA who is signature on the account. However, all brand inspection employees are employees of the SDSGA and they pay inspectors' salaries and or contract fees and then one lump sum check for payroll is written on the SDSBB account to the SDSGA account to cover payroll expenses. As a concession to the SDSGA to

gain the financial transparencies, the SDSBB guaranteed the SDSGA 8% of all inspection fees collected as profit for running the program. That fee is called an implementation fee and will equal approximately \$70,000 to \$90,000 per year depending on the number of animals inspected and the per head fee charged.

The new contract's time frame presents somewhat of a problem for this analysis since the first year of the contract will not end until June 30, 2008, therefore a full year's history is not yet available. Thus in analyzing financial information and the feasibility of the SDSBB taking over the brand inspection program the Consultant looked at the calendar year of 2007 by combining January 1, 2007 thru June 30, 2007 financial information under the old contract with July 1, 2007 thru December 31, 2007 information under the new contract. The Consultant assumed that for analytical purposes the new contract was in force for the entire calendar year of 2007.

A significant part of the study's analytical work will be found in various exhibits attached to this report and are taken from several Excel spreadsheets created by the Consultant from information provided by the SDSBB and the SDSGA. They are identified and labeled as follows:

- Exhibit A – Assumptions
- Exhibit B – Brand Inspectors' Compensation as State Employees
- Exhibit C – Income
- Exhibit D – Expense
- Exhibit E – SDSGA Expenses
- Exhibit F – Local Inspection Income & Expense Scenarios
- Exhibit G – Explanation of Belo Employment Contracts

Exhibit A shows a total of 52 assumptions, facts, calculations and/or estimates made by the Consultant based on information provided by the SDSBB or the SDSGA. Some of the estimates are just that and are not presented as being factual but were made in order to determine some information that was not readily available. Although these estimates may or may not all be accurate they do not drive the ultimate conclusions or recommendations of the study.

Exhibit B of the study is a critical part of the entire project. Although there are various expenses associated with providing the brand inspection services, 76% of the current budget agreed to by the SDSBB and the SDSGA represents direct employee costs. An additional 10% of the budget represents direct mileage paid, lodging and meals for a total of 86% of all expenses relating to the cost of people to provide the service. This exhibit assumes that the employees became SDSBB employees and presents various scenarios regarding compensation. The Consultant worked with the South Dakota Department of Personnel to determine the salary grades that employees would fall under and was provided a high, low and then calculated and average compensation for each grade and type of employee including benefits.

Exhibit C shows the income portion of a profit and loss statement. The Consultant used the current Fiscal Year 2008 budget that was agreed to. In order to develop actual revenues the Consultant used the actual income from January 1 thru December 31 of 2007. The last 2 columns show a best case budget for income and a conservative budget. There will be more discussion on the projected budgets for both income and expenses later in the report.

Exhibit D shows the expense portion of the profit and loss statement and as with the income the Consultant used the current operating budget, actual 2007 calendar year expenses and presents two alternative expense budgets. There will also be more on this exhibit later in the text.

Exhibit E shows various expenses in the first half of 2007 that under the old contract the SDSGA charged to the brand inspection programs which are not covered under the new contract or in the budget. In some cases, the SDSGA still has those expenses but they are now covered by the 8% implementation fee and covered by the SDSGA.

Exhibit F is an analysis of local inspections. For various reasons this will be talked about later because local inspections may be affected more by a transfer of management to the State than will market inspections. This exhibit shows various expense and income scenarios that will be discussed later in the text.

Exhibit G is an article written by Robert Ditmer that explains how Belo employment contracts may be used by an employer for employees whose work weeks vary above and below 40 hours per week. The SDSGA uses the Belo contracts for all full time inspectors.

There are several issues that may impact costs if the SDSBB were to take over the brand inspection program which could in turn affect inspection fees and related income. There are other costs that should not change regardless of who is managing the program. This discussion will break those down by program area and type of employee.

Administratively, unless the SDSBB was to change the brand inspection program, the costs to administer the program should not change significantly. The state would need a Chief Brand Inspector or Program Administrator to manage the overall program. He/she would need a full time assistant to handle inspection records and a part time accounting clerk to assist with the financial transactions. The SDSBB may need some additional office space but that cost should be less than the \$15,000 currently paid to the SDSGA. Telephone, office equipment and other general office expenses should remain about the same as they are currently being incurred and budgeted.

The SDSGA currently pays full time inspection employees a salary that is paid under a Belo employment contract (Exhibit G). A Belo contract can only be used under Federal Law if certain conditions are met. The main condition is that an employee's hours varies each week above and below 40 hours and that variation is driven by the work being performed and is not driven by the employee or employer. Because of the seasonal nature of cattle movement, brand inspection certainly meets that requirement. Other limitations include a maximum number of 60 hours before overtime must be paid and based on the maximum number of hours agreed to by employer and employee the compensation must be at least minimum wage. The agreements with the full time brand inspectors and the SDSGA meet all of the tests of the Belo contract and based on the research conducted by the Consultant they could be executed by the SDSBB in the same manner being done at the present time.

Market Inspections

The cost of performing the market inspections at the 17 current markets will change somewhat primarily due to health insurance cost paid by the State for all full time employees. Currently the SDSGA offers a health insurance plan but is paid entirely by the employee to the insurance carrier and is not shown in the budget analysis. If the State were managing the program they would pay \$5,700 per year for the employee starting July 1, 2008 and is shown as a part of the budget analysis. In addition full time employees would be eligible for the State retirement plan which is a part of the estimated 14% payroll burden shown in the analysis. Currently employees have a 401k that they can participate in and the SDSGA matches the employee contribution up to 3%.

Full time employees are aided at markets by part time inspectors who are paid a day rate currently at \$90/day plus mileage and a meal allowance of \$12 per day. Since that rate is well above minimum wage that cost would not change. The State requires that if an employee works more than 20 hours a week for 6 consecutive months, they are then entitled to benefits including health insurance and the State retirement program. It appears the average number of days worked per year by part time inspectors is 31 with most of that time in the Fall or Spring so they would not be eligible for those benefits. Currently part time inspectors are paid as contract employees and provided a 1099 at the end of the year. There is no reason to believe that the State would handle them differently.

Local Inspections

Local inspections become a more complicated analysis. Local inspections are performed by full time, part time and local inspectors. Full time inspectors are paid their salary and do not receive any additional compensation to perform a local inspection. It is in the best interest of the SDSBB, under the current contract, not the SDSGA, to perform as many local inspections as possible using full time inspectors. However one problem with managing that is a producer

wanting an inspection usually calls the inspector directly and the SDSGA does not know that the inspection took place until after the fact when the paper work arrives at their office.

All inspectors who perform local inspections collect \$.80 cents per head inspected and \$.37 per mile to and from the inspector's home at the time of the inspection and send it with the paper work to the SDSGA office.

The SDSGA pays part time and local inspectors \$.35 per head inspected and \$.37 per mile for local inspections. In other words they are paid by the piece. Local inspectors for the most part only perform local inspections and they average about 68 inspections per year per inspector at an average head count of 39. However they appear to perform nearly 80% of all local inspections. Based on the actual 2007 mileage revenue from local inspections divided by \$.37 per mile the average local inspection is about 11 miles round trip for the inspector. Therefore a local inspector is paid \$13.65 plus \$4.07 for mileage for the average local inspection performed. If everything goes as planned (which it probably does about 50% of the time) the inspector can leave home, perform the inspection and be home in an hour and not more than two hours.

This part of the program is currently being examined by the State wage and hour auditors and may be subject to some changes to insure the inspector is being paid at least a minimum wage. For inspections of less than 19 head the inspector would not receive minimum wage for one hour of work. The South Dakota Office of Personnel will not give a concrete answer at this time but is inclined to advise the Consultant that at least a minimum wage may be required if they were working for the SDSBB. We will review this in more detail when discussing the income and expense budget later. The State of South Dakota may also require the SDSGA to do the same. If that is the case, this may not be an issue in the SDSBB assuming the program, because the costs would be the same.

It is harder to analyze the local inspections performed by part time inspectors because for the last 6 months of 2007 there is no differentiation in compensation they were paid for market inspection support and local inspections. Part time inspectors doing local inspections would fall under the same policies as local inspectors.

Income Budget Analysis

Exhibit C shows the 2008 fiscal year fee income budget agreed to by both parties at \$1,120,000 and calendar year 2007 actual at \$1,072,224. The difference can easily be explained by the difference in the two twelve month periods that was observed.

The projected income budgets prepared by the Consultant differ only from actual in the amount of revenue projected from local inspections. The conservative

budget uses the current \$.80 per head as the projected revenue. The best case budget uses the Colorado system of \$10 per local inspection plus the per head inspection fee of \$.80 per head and eliminating the mileage charge to the producer. As shown in Exhibit F the conservative budget anticipates no change from current policies. The best case budget assumption shows an increase of \$87,000 in fees but a decrease in mileage revenue of \$45,000 or a net increase in revenues of \$42,000.

The inspection fees charged should be based on actual costs of the program. The goal of brand inspection is not to make a profit but to deter theft through inspection and to return strays to the rightful owner of the livestock. The Consultant is not suggesting that an increase in fees is needed at this time. However, to generate a similar increase in revenue that the Colorado system would provide would require the inspection fee be increased to \$.90 per head on all animals inspected.

There are several options that the SDSGA or the SDSBB could consider to increase revenues if the cost of inspection warranted an increase. Those include a minimum charge on local inspections, an increase in the inspection fee to a higher amount than \$.80 per head or even a varying fee between market inspections and local inspections which could be justified based on cost of the inspections. If either party were to charge something other than a flat per head fee it may require seeking legislative authority before it could be considered.

Expense Budget Analysis

There are several differences in the expense budgets and projections. First the administrative compensation compares the 2008 fiscal year budget to the 2007 calendar year actual and the projections based on the program being administrated by the SDSBB. The budget is \$105,000 and the 2007 actual is \$100,211. The comparison is well within budget. The projections are based on the assumption that the Chief Inspector would grade at a N16 with a range in hourly compensation between \$16.52 and \$20.65. The Administrative Assistant would grade a N09 with a range in compensation between \$9.02 and \$11.27 and a part time accounting clerk at half the Administrative Assistant's compensation at the same grade. This would project a savings of \$22,000 to \$38,000 compared to the 2007 actual. The grades that were used may or may not be correct but the bottom line is administrative compensation costs if the SDSBB assumed the program would be less than current costs. In addition the employees would all receive health insurance at the State's expense and valued at \$5,700 per employee. That cost is recognized later in the analysis.

Currently compensation for the 15 full time brand inspectors is slightly over \$29,000 per year per employee. That total is just over \$439,000 for 2007 with a budget of \$440,000 for FY 2008. The projections if the SDSBB assumed those salaries based on a grade of N14 with an hourly range of \$13.50 to \$16.88 would

be \$28,000 to \$35,000. Again the employees would receive health insurance at a cost to the State of \$5,700 per employee where today that is the employee's expense. At the high end of the range the total cost would add \$87,000 or at the low range lower costs by nearly \$19,000. Depending on inspectors transferring to the SDSBB the actual cost probably lies somewhere between the two numbers.

Part time inspectors are proposed to have a salary range based on their grade of \$11.25 and \$13.50 per hour. The low end of the range is almost identical to the total compensation paid to part time inspectors and the high end would increase the costs by almost \$18,700. Basically no part-time inspectors would qualify as full time employees and thus would not be entitled to State benefits. The bottom line is that part-time inspector's compensation would be basically neutral between a SDSGA or a SDSBB administered program.

Local inspectors conduct the vast majority of local inspections. The budget for the 2008 fiscal year is \$135,000 and the actual expense for 2007 is \$108,463. The projections for the budget if the SDSBB were to take over the inspection program have several assumptions embodied in the numbers. The conservative case assumes that local inspectors would be paid \$10 per inspection for less than 20 head and for all inspections greater than 20 head they would receive \$10 plus \$.35 per head for all head counts over 20 head. The best case scenario assumes that they would be paid a flat rate of \$8.00 per hour with a minimum of 2 hours per inspection. The best case totals \$136,584 slightly over the \$135,000 budget for FY 2008 and over the actual 2007 expense by \$28,000. The conservative case reflects a total expense of \$155,342 which is about \$19,000 over the best case.

If the South Dakota wage and hour auditors conclude that the local inspections conducted by local and part time inspectors must receive at least a minimum wage for all inspections the result should be no different regardless of who is managing the inspection program.

The bottom line for employee compensation is that the current FY 2008 budget is \$783,500 and the actual for calendar year 2007 was \$751,832. The conservative projected budget if the SDSBB administered the program would increase costs over actual 2007 costs by \$120,000 and if the best case were to be implemented it would save \$38,000. Again depending on the results of the current audit being conducted by the State this issue may have a neutral affect regardless of who is directing the program.

There would essentially be no impact on employees or program cost as it relates to travel expenses whether the program is administered by SDSGA or SDSBB. The SDSBB operating under South Dakota State policies and currently the SDSGA pay \$.37 per mile which is what is allowed by the State and reimburse employees basically at cost for meals and lodging.

As mentioned earlier there will be some impact on employees and program costs if the program were operated by the State and the SDSBB. The primary impact will be in the retirement program of the State versus the 401k currently offered by the SDSGA. The State will require a 6% contribution to the retirement program while the 401k program is voluntary. Currently the SDSGA is matching 5% of the total full-time employee's compensation and since they only match up to 3% it simply means that some part-time and/or local inspectors are participating in the 401k. Under the State the part-time and local inspectors, as long as they do not reach full time status, will not be able to participate and full-time employees will have to participate. Thus to the extent some full-time employees are not participating in the 401k up to 6% they will realize a decrease in take home pay. However the costs to the program based on this analysis will have very little impact under the two operating scenarios.

The health insurance policies will have the opposite effect of the retirement program. Starting July 1 the cost of the health insurance offered by the State would cost the SDSBB \$5,700 per employee per year. That will increase the cost of the program an estimated \$96,900 per year. However the full-time employees will benefit because currently the SDSGA offers a voluntary health insurance program at the employees' expense. Part-time and local inspectors will not be able to buy the health insurance under the State unless they become full-time. So to the extent that part-time and local inspectors are buying the health insurance offered by the SDSGA they will lose that opportunity.

Insurance, office, and other expenses in 2007 at the SDSGA totaled slightly more than \$82,000. These costs would be reduced somewhat under the State and are projected at about \$64,000. These expenses are itemized in Exhibit D. The SDSBB would pay 2% to the State of all operating expenses for payroll, legal, audit, insurance and other services. These expenses are line items in the 2007 actual expenses incurred by the SDSGA.

The bottom line of this analysis is presented in the table below

<u>Profit & Loss Summary of 4 Scenarios</u>				
	<u>2008 FY Budget</u>	<u>2007 Actual</u>	<u>Conservative Projected</u>	<u>Best Case Projected</u>
Income	\$ 1,175,400	\$ 1,107,915	\$ 1,126,595	\$ 1,168,655
Expense	\$ 1,174,230	\$ 1,088,534	\$ 1,235,722	\$ 1,057,098
Profit/Loss	\$ 1,170	\$ 19,381	\$ (109,127)	\$ 111,558

The 2008 FY budget includes the 8% implementation fee paid to the SDSGA and with that is essentially a balanced budget. If the first half of 2007 is an accurate projection of the first half of 2008 the program should show a slight profit of nearly \$20,000 which will accrue to the SDSBB under the terms of the current contract.

The projected budgets reflect conservative revenue and liberal expense projections in the conservative budget and more liberal income and conservative expense projections in the best case projected budget. The truth and reality probably lies someplace in between the two scenarios. Although revenue projections between the two are slightly different the main difference can be explained in compensation and benefits for employees. The conservative projection uses the top range of the salary grade and the best case uses the low range and that is why reality is somewhere in between because some full time inspectors may be paid at the high end and some would be compensated at the lower end of the range depending on length of service and experience.

Industry Politics

As mentioned earlier in the report the SDSGA has contracted with the SDSBB to perform the brand inspection service in the West River brand inspection area since basically the beginning of the program. The SDSGA is not the only State cattlemen's association in South Dakota. They have a rival to represent cattlemen's interest in the State with the South Dakota Cattlemen's Association (SDCA) headquartered in Pierre, South Dakota.

In the mid 1900's the SDCA was generally recognized as a cattle feeder's organization and was affiliated with the National Livestock Feeders Association (NLFA) located in Omaha, Nebraska. At that same time the SDSGA was generally considered the cow-calf and range producers organization and affiliated with the American National Cattlemen's Association (ANCA) located in Denver, Colorado. In the 1970's the NLFA merged with the ANCA to form the National Cattlemen's Association with offices in Denver, Omaha and Washington DC. At that time both the SDSGA and the SDCA affiliated with the NCA.

In the mid 1990's the NCA merged forces with the National Livestock & Meat Board's (NLMB) Beef Industry Council (BIC) located in Chicago, Illinois to form the National Cattlemen's Beef Association (NCBA) with offices in Denver, Chicago, and Washington DC. Up until the merger the NLMB since the 1920's had been the beef, pork and lamb industry's product promotion, research and information organization and had been supported by various National and State check-off programs. This merger was somewhat controversial in the industry with some feeling that there was more efficiency with one industry voice rather than two and those that felt the industry policy and governmental lobbying efforts should remain separate from the industries product promotion efforts.

In the late 1990's three primary issues caused division among cattlemen at the State and National level. Those issues revolved around foreign trade, live cattle marketing and packer cattle ownership issues, and those that were in favor of and those that were opposed to the \$1/head National Beef check-off mandated by Congress in the mid 1980's. These differing view points led to the formation of a rival national organization called R-Calf headquartered in Billings, Montana.

In general cattlemen and their State Affiliates that opposed free trade supported country of origin labeling (COOL) on meat products, and a packer ban on owning livestock prior to slaughter, and opposed the \$1/head check-off affiliated with R-Calf and those of the other point of view remained with NCBA.

When the split happened State Cattlemen's Associations had a choice to make as to who they would affiliate with at the national level. After a period of time the SDSGA elected to affiliate with R-Calf and the SDCA remained affiliated with NCBA. It should be pointed out that the issues that divide the two national organizations are emotional and divisive issues that both sides are passionate about and that passion carries over at the State level. It also should be pointed out that the SDCA has broadened its appeal and works to attract like minded cattlemen as members regardless of their cattle industry sector. The same should be said for the SDSGA. Both have members East and West of the Missouri River however the majority of SDSGA members are West River and the majority of the SDCA members are East River.

Why is this important to the discussion regarding brand inspection? East River cattlemen tend to be neutral or opposed to mandatory brand inspection and West River cattlemen tend to support mandatory brand inspection so it is logical to assume that their associations share that point of view. It is also logical to assume that SDCA members resent profits from brand inspection accruing to the SDSGA under the old contract or from the 8% implementation fee in the new contract are used to further advance positions on other controversial issues.

The position of the Consultant is not to pick sides between the industry organizations at the National or State level but to point out that these differences are real and in all likelihood will continue in the foreseeable future. To the extent that these issues spill over into the State legislature and other political bodies in the State they will continue to be divisive for brand law and inspection related policies in the State. Some feel that reasonable cattlemen when they set down to debate and determine brand related policies whether in the SDSGA, SDCA, SDSBB or legislative forums will not let other issues cloud their views on brand and inspection policies. Those that read this report and make future decisions will have to make that call.

Cost and Benefits of Brand Inspection to the Industry

Jim Reed, Chief Brand Inspector for the SDSGA was very precise and concise when asked what the purpose and objectives were of the brand inspection program when he stated:

- To deter theft through brand inspection
- Return strays to the rightful brand owner

The following chart attempts to quantify the value of the second objective for South Dakota Cattlemen for 2007.

Data and Cost Calculations		
Annual Program Cost - 2007 Actual	\$	1,088,534
Total Number of Animals Inspected - 2007		1,389,002
Total Market Holds for Proof of Ownership - 2007		24,656
Holds to the SDSGA & Paid to Brand Owners - 2007		287
Holds Forwarded to the SDSBB - 2007		16
Cost Per Animal Inspected	\$	0.78
Cost Per Animal Held to Prove Ownership	\$	44.15
Cost Per Animal Held Sent to SDSGA	\$	3,792.80
Cost Per Animal Sent to SDSBB	\$	68,033.34

In 2007 a total of 24,656 head of livestock were held at markets out of the 997,008 head inspected at the markets, until proof of ownership could be determined. Proof of ownership was determined on all but 287 animals within 60 days and likely most were determined within hours or a couple days of being presented for sale. Information is not available on how much ownership was proven by the person that delivered the cattle for sale or to another party. If you put the total cost of the program against those 24,656 head, the cost was \$44.15 per head. After the 60 day hold period at the market, 287 head were forwarded to the SDSGA. The SDSGA and the SDSBB have up to one year to prove ownership after that point in time. If we applied the program cost total to that number the benefit cost was \$3,792.80 per head. Of the 287 where ownership was not proven, 16 were forwarded to the SDSBB where they have the remaining time left in the year since they were forwarded to the SDSGA to prove ownership. If total program costs were applied to that number the cost is \$68,033.34 per head.

Those that use this report to make decisions can draw their own conclusion as to how the brand inspection program should be valued by the industry. Frankly more information would need to be collected in order to determine true costs based on strays returned to the rightful brand owner.

It is much more difficult to determine the value of the program in theft prevention. No data exists to place a monetary value and only subjective conclusions can be drawn. If years of data were available on thefts reported to the SDSBB from East versus West River some conclusions may be drawn, however to the Consultant's knowledge that information is not readily available.

Alternatives That Could Be Considered

Whether the program is managed and operated by the SDSGA or the SDSBB several program changes or improvements should at least be considered and opened up for debate and resolution. These issues are listed with the Consultant's comments on each.

1. Consider expanding brand inspection Statewide:

Comment – Over the years this issue has been debated several times. The Consultant is not aware of any movement by East River cattlemen to have the entire State declared a brand inspection area. The facts are that more than 80% of cattlemen West River brand and only 20% plus brand East River so it would appear that brand inspection would add very little value and/or benefit to the industry East River. The Consultant would not recommend this action as a viable alternative.

2. Consider eliminating brand inspection West River:

Comments –

- North to South and other States' policies and programs:
 - North Dakota – State wide brand inspection
 - Nebraska – Western portion of the State has inspection and the eastern portion has no brand inspection.
 - Kansas – Has a couple counties in the western portion that have inspection and the balance of the State relies on investigating reported thefts in the Brand Commissioner's office.
 - Oklahoma – No brand inspection and investigates reported thefts.
 - Texas – Brand inspection at markets only and investigation are both provided by the Texas Southwest Cattle Raisers Association and the inspectors are certified law enforcement officers.
- All of the above States have brand registration laws where it is unlawful to apply a brand unless it is registered. For the most part all States west of the above have brand registration and inspection before the livestock can leave a brand area. The States east of the above States have no brand inspection and some do not even have brand registration laws.
- Brand inspection in the Western States is a tradition and those of current and past generations grew up with it and accept it. However times and practices have changed and there are States east of the States above that have substantial cattle industries and have survived and flourished without inspection and as far as the Consultant knows do not have any higher rate of cattle theft than Western States. Granted, States in the east are more populated with smaller pastures and a more gentle terrain while the States in the west are very sparsely populated with large pastures and much rougher country.
- It is the opinion of the Consultant that this option should at least receive some thoughtful discussion.

3. Consider brand inspection West River at markets only and eliminate local inspections:

Comment – This approach seems to work in Texas. If it were adopted, the SDSBB should investigate methods to significantly enhance the investigative resources. There are many law enforcement techniques that could be utilized to deter theft and minimize the impact of eliminating local inspections.

4. Consider eliminating all horse inspections:

Comment – The horse inspection program adds very little revenue and according to the Chief Brand Inspector creates more questions and problems than any other part of the program. This should receive priority consideration regardless of who is managing the inspection program.

5. Shipper's permits are issued by shipper's agents at no charge to the producer if he is transporting livestock out of the inspection area to a designated "open market".

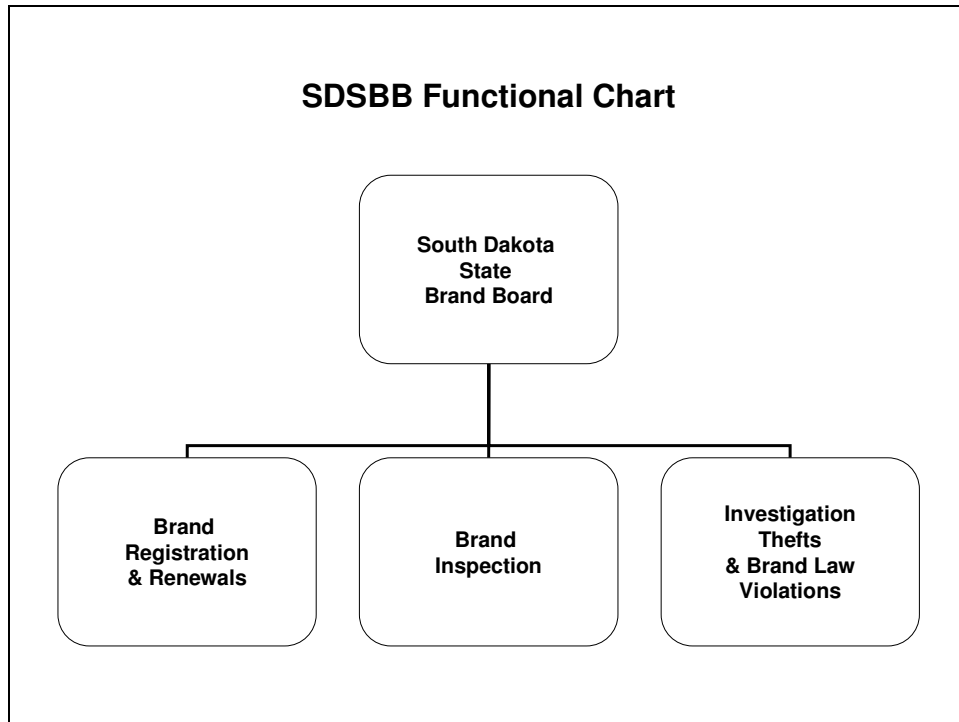
Comment – The entire process should be evaluated because it appears that the delay in paperwork and the process to write a permit may not provide the intended value or benefit.

Summary & Conclusions

The primary question to be answered by this study is: Is it financially feasible for the SDSBB to take over the brand inspection program and manage it along with the brand registration and the theft and violation investigative programs they currently operate. The simple answer to that question is yes.

The financial analysis included in this report identifies the differences between the programs being contracted to a private contractor (SDSGA) versus being managed by SDSBB. From a pure cost standpoint there are advantages and disadvantages under either scenario. The primary differences in cost of the program are that the SDSBB would pay the health insurance costs for full time employees that the SDSGA do not currently pay. However, that is a benefit to the full time employees. On the other hand, the program would eliminate the 8% implementation fee as a program cost if the program were managed by the SDSBB. Those two costs balance each other out and although there are other differences in various line items, the bottom line remains that financially the State should be able to operate the program as or more efficiently than an independent contractor.

There are some opportunities if the SDSBB were to assume the administration of the program. Following is a proposed functional chart and later a staff organizational chart for the SDSBB if they were to assume brand inspection responsibilities.



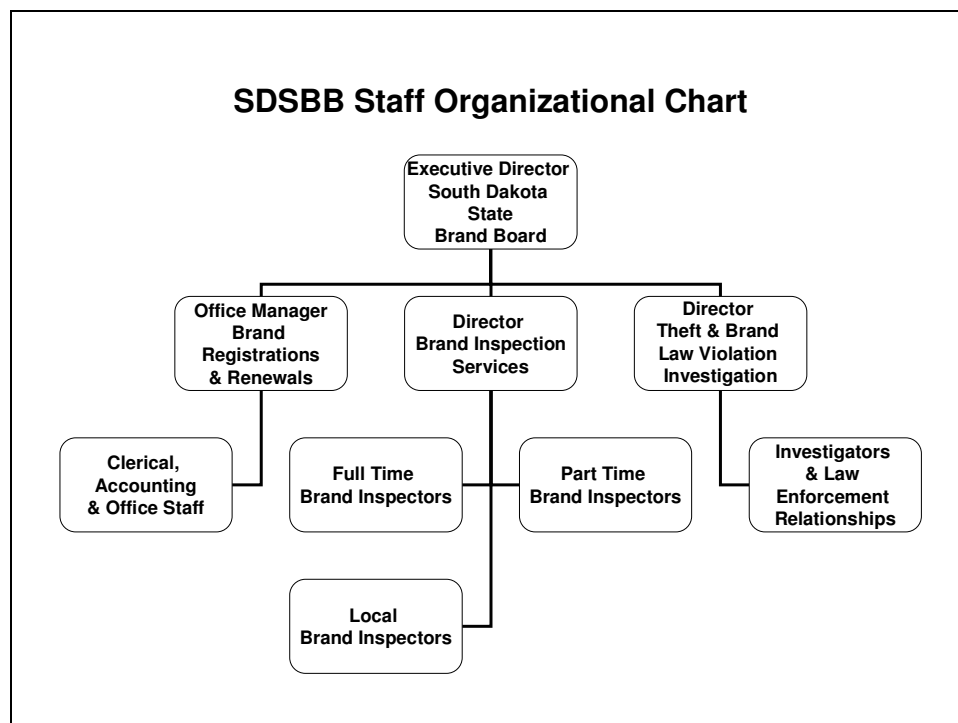
There is certainly some efficiency that could be captured by all of the State's brand registration, inspection, and investigative powers being under one board and management structure. The cost may not be reflected in less manpower but more in the ability to utilize the employees in a more efficient manner. The second advantage that could produce benefits in the industry is in the area of communications and sharing of information between the inspection program and investigators.

It appears to the Consultant that there is a "hand-off" without a "hand-shake" when dealing with brand inspection law violations and to some degree with theft investigations between inspectors and investigators.

For example the best case scenario when a probable theft is discovered by a producer is that he immediately calls the local law enforcement agency, probably the county sheriff, and reports the theft. At that point the producer or the county sheriff should call the SDSBB investigative branch to also report the suspected case. In the ideal world the brand inspection office would also be notified or if a local inspector was called he notifies the Chief Brand Inspector. The local law enforcement officer is in the best position to capture at the site any evidence that may be available that could lead to a suspect. However the SDSBB investigator or the Chief or local Brand Inspector may have information that could be helpful to solve the crime. The point is that timely and total collaboration should happen to have the best possible odds of solving the crime.

Currently the Sheriff is responsible to the county, the Chief Brand Inspector is responsible to the SDSGA and the Chief Investigator is responsible to the SDSBB. The current structure creates structural barriers that regardless of great intentions by all parties tends to break down in many cases. People are people and they all have their jobs to do and if the primary responsibility for something is someone else's they may not always act in a timely manner. Several incidents were cited by both parties during this study that the other party may not be doing their job in the area of theft and brand violation investigation. If inspection and investigation were organized in one management structure at least one barrier for full cooperation and collaboration is eliminated. The industry is paying the bill through fees and is the party that suffers when the responsible organizations do not work together as a team.

An old lesson in livestock judging is that form follows function and the same applies in organizational structure. The following chart outlines the staff form chart to fit the functional chart above. This chart does not contemplate major changes in how the programs would be operated but simply puts them in one organizational structure. The top four positions in this chart should be located and officed in the same place. Daily and or weekly coordinating meetings could then be held to serve the industry in the most efficient, and more importantly, effective manner. Obviously a chart is just a structure and filling the positions with the right people who are qualified and dedicated to serving the industry is the most important step to future success.



One more point should be made if the above structure or something similar were to be implemented. Since all employees would become State employees, some brand inspectors strategically located could also be certified as State law enforcement personnel and become part of the investigative staff while continuing as inspectors. This may help relationships with local law enforcement agencies since they would be more local and acquainted with each other. The point is, even this structure does not incorporate local law enforcement agencies. Steps should be taken to build relationships with local law enforcement agencies to provide the best service possible to the livestock industry.

Recommendations

- The SDSBB should give serious and thoughtful consideration to bringing the brand inspection program under its management. As pointed out earlier, it is economically and financially feasible. In addition, the political climate will continue to place a cloud over the program as it exists today.
- The Consultant suggests that if the contract is renewed with the SDSGA in 2008 for another year that the SDSBB consider giving immediate notice to the SDSGA that it will not be renewed in 2009. Such a notice would not prevent the contract from being renewed for another year if both parties agreed but would give all parties ample time to prepare for an orderly transition of the program as well as the SDSGA time to prepare to operate without the brand inspection service.
- The Consultant has had experience with producer attitude surveys in the past and believes that if the SDSBB follows the two recommendations above there would be ample time to develop a survey. It could be sent to a statistically sound sample of brand registration holders, producers, market owners and operators, and others in the industry to gain valuable input in the decision making process. There are other stakeholders in the brand inspection program in South Dakota that should also be solicited to get their thoughts and expectations.
- The horse inspection program appears to add very little value for horse owners and seems to require more time and headaches than the fees generated. All parties should give serious consideration to its elimination.
- As mentioned earlier in the report the Colorado fee structure for local inspections of a flat minimum fee for every inspection plus a per head charge on every animal inspected would be a preferred method. The mileage charge to the producer could be eliminated and based on the mileage income received in 2007 the flat fee would more than cover that cost paid to the inspectors.

- The program should exercise more coordination in scheduling local inspections to maximize the use of full time inspectors and lower program costs and to improve the quality and integrity of the program.
- Some other States use various forms of computers and electronic tools that are now available in commerce. It seems that these technologies should be identified and studied to understand what efficiencies could be gained by their use and how service might be improved.

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Jim Reed Chief Brand Inspector in the SDSGA office was extremely cooperative in spending the necessary time to educate the Consultant on every aspect of the brand inspection program. He was also very helpful in finding and getting the information requested in a timely manor – Thanks JIM

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Exhibits

Exhibit A – Assumptions

Exhibit B – Brand Inspectors' Compensation as State Employees

Exhibit C – Income

Exhibit D – Expense

Exhibit E – SDSGA Expenses

Exhibit F – Local Inspection Income & Expense Scenarios

Exhibit G – Explanation of Belo Employment Contracts